JAMES R. BROWNING, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 22[illegible]

LEWIN WETHERED, TRUSTEE OF THE ESTATE OF JOHN B. GAITHER, JR., INC., BANKRUPT,
Petitioner,

v.

ALBAN TRACTOR COMPANY, INC., HERBERT L. WYNNE, TRUSTEE, AND PLAZA CORPORATION,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

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PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

Lewin Wethered, Trustee of the Estate of John B. Gaither, Jr., Inc., Bankrupt, prays that a writ of certiorari issue to review the decree entered in this cause on April 13, 1961, by the Court of Appeals of Maryland.

OPINIONS BELOW

The opinion of the Court of Appeals of Maryland (Appendix B) is reported at 168 A. 2d 358. The opinion of the Circuit Court No. 2 of Baltimore City (printed at pp. 23-44, incl., of the Record Extract in the Court of Appeals.

copies of which are furnished with this Petition) is reported unofficially in The Daily Record (Baltimore, Md.), for March 19, 1960.

JURISDICTION

The decree of the Court of Appeals of Maryland, which is here sought to be reviewed, was filed March 9, 1961, and the petitioner here filed motions for modification and reargument on April 7, 1961, which were denied on April 12, 1961, following which the mandate and transcript were forwarded to the Lower Court by the Clerk of the Court of Appeals of Maryland on April 13, 1961. The jurisdiction of this Court is invoked under U.S. Code, Title 28, Section 1257(3).

QUESTIONS PRESENTED

The questions in the case relate to the right of a Trustee in Bankruptcy to avoid an unrecorded chattel mortgage of the now bankrupt mortgagor on which foreclosure proceedings had been instituted and a sale of the mortgaged property made many months prior to the commencement of bankruptcy, but after Federal taxes and interest were assessed against the mortgagor, which, Petitioner contends, gave rise to a lien on that property entitling him to avoid the mortgage and the foreclosure proceedings by and under Section 70(e) of the Bankruptcy Act. These questions are:

ONE: Under Internal Revenue Code, Section 6321, is a prior demand for payment of interest a prerequisite to the creation of a Federal tax lien, particularly a lien for interest?

TWO: If this question be answered affirmatively:

A. Can such a requirement be waived by the taxpayer, or, in the alternative, satisfied by the taxpayer's knowledge

of the amount due coupled with (and as evidenced by) tender of a bad check in payment?

B. Can same be satisfied under a doctrine of "relation back" by the subsequent formal claim of the Federal Government in other legal proceedings?

THREE: Under Section 6323, Internal Revenue Code, does notice of a Federal tax lien have to be duly filed to be valid as against a precedent mortgage improperly recorded? Or, in the alternative, does a prior unrecorded mortgage prevail over an unfiled Federal tax lien.

(NOTE: This involves the decision of this Court in *United States v. R. F. Ball Construction Co.*, 355 U.S. 587, 78 S. Ct. 442, 2 L. Ed. 2d 510.)

STATUTES INVOLVED

The applicable provisions of the Internal Revenue Code (26 U.S.C.A. Sections 6321, 6322, 6323 and 6601) and of the Bankruptcy Act (11 U.S.C.A., Section 70(e)) are printed in Appendix A, infra, pp. 11-13, inclusive.

STATEMENT OF THE CASE

Petitioner is Trustee in Bankruptcy of John B. Gaither, Jr., Inc., a now defunct Maryland corporation.

In May, 1955 Alban Tractor Co., Inc., sold Gaither certain equipment upon which Gaither executed a mortgage to Alban. It was recorded in Baltimore City, not in Baltimore County (a separate political jurisdiction), where as court decisions later revealed, local law required recordation for this mortgage to be valid against protected classes of persons named in that law.

On August 22, 1956, the United States entered an assessment against Gaither for delinquent taxes in the amount

of $5,705.32, penalty of $285.87 (for late filing), and interest from the due date of July 31, 1956, to the date of assessment in the sum of $19.19. In fact, Gaither had paid the $5,705.32 on August 14, 1956. If credit had been then allowed for this payment, that would have left due the penalty and interest totaling $305.06.

On November 5, 1956, Alban filed a petition in the Circuit Court No. 2 of Baltimore City to foreclose the mortgage then in default. The foreclosure sale was held December 1, 1956, and certain creditors of Gaither's filed exceptions to its ratification. Pursuant to a stipulation, the sale was later ratified on June 6, 1957.

The United States filed notice of its tax liens (including that of August 22, 1956) in Baltimore City on December 27, 1956, and in Baltimore County the next day. Meanwhile, Gaither undertook to pay the amount of $305.06 by a check received November 14, 1956, by the District Director's office. This was not paid when presented and the following day (November 15, 1956) Gaither made a deed of trust for the benefit of its creditors. It was recorded in Baltimore City preliminary to assumption of jurisdiction of that matter by the local court. Many months later, the Court of Appeals of Maryland held in a decision on March 5, 1958, that Gaither's legal corporate residence was Baltimore County. Under local law, the latter, and not Baltimore City, was thus the proper place for recordation of the deed of trust and the chattel mortgage.

Following that decision (*O'Toole Tire Company v. John B. Gaither, Jr., Inc.*, 139 A.2d 252, 216 Md. 54), (which invalidated the deed of trust for the benefit of creditors) Gaither was adjudicated a bankrupt on May 12, 1958, and the petitioner appointed trustee in the bankruptcy case.

His efforts to capture the proceeds of the foreclosure sale then began and continue to this time.

Still later, the Court of Appeals held in another case (*Plaza Corporation v. Alban Tractor Company, Inc.*, 151 A. 2d 170, 219 Md. 570) between Alban and a competing mortgagee (Plaza) that Alban's mortgage was not recorded as required by Maryland law.

The Court of Appeals of Maryland in its decision which Petitioner asks this Court to review (Appendix B commencing at p. 14) held, inter alia:

> A. "There was no Federal lien because that government made no demand upon Gaither for payment of any tax (a mandatory, statutory prerequisite to the creation of such a lien) at a time when Gaither had any property or rights of property to which a lien could attach" (Appendix B, p. 19).
>
> B. "The interest included in the amount of $305.06 specified in the notice of lien duly recorded is provable in bankruptcy but no lien ever arose as to it because it was never demanded to be paid. Section 6321 creates a lien only if a person owing a tax 'neglects or refuses to pay same after demand.' " (Appendix B, p. 22).
>
> C. "Nor do we reach the question whether when Section 6323 says the Federal lien shall not be valid as against 'any mortgagee' until notice of the lien has been filed, it includes a mortgagee under an unrecorded mortgage, that is, whether a nonstatutory contractual lien must be choate and perfected to prevail. The Supreme Court has never given an explicit answer" Appendix B, p. 26. (NOTE: there follows a consideration of the *Ball* case, supra, pp. 27, 28).

On questions ONE and Two, Alban's counsel argued in the trial court that no lien was established prior to the foreclosure because no interest was demanded to be paid. However, that court only referred to this point in com-

menting that the first demand was on August 22, 1956, going on to hold that no lien would be valid as against the mortgagee until notice thereof had been filed as provided by Section 6323(e) (E. 37). In Respondent's Brief on appeal this point was raised again and answered by the within Petitioner in his Reply Brief and Motion for Modification and Reargument.

On question THREE, as the quotation at B indicates, the Court of Appeals did not decide the question, although it had been adjudicated in the trial Court.

While the quotations at A and B answer our question ONE affirmatively (and, we submit, erroneously), there is absolutely nothing in the Lower Court's decision on questions Two and THREE which were presented originally in Petitioner's Reply Brief and renewed in his Motions for Modification and Reargument.

REASONS FOR GRANTING THE WRIT

The primary reason for granting the writ is that the Court of Appeals of Maryland has decided Federal questions of substance not heretofore determined by this Court, namely, whether demand is a mandatory requirement of a Federal tax lien, particularly, one for interest on taxes due; whether any such requirement can be waived by the taxpayer or satisfied upon his tender of payment; and whether such requirement can be satisfied by the subsequent filing of the tax claim in a legal proceeding.

That Court has cited a number of lower Federal Court decisions as holding that there must be a demand (Appendix B, pp. 22, 23) of the tax in order for the lien to follow for that tax. This is not authority that there must be a demand for interest, as such, which accrues automatically from the date of underpayment at the rate of 6% per

annum (26 U.S.C.A. Sec. 6601 set forth at Appendix A, pp. 11, 12). Not only is a taxpayer charged with knowledge of this statute as a matter of law, but, we submit, the provision is known to most as a matter of fact.

If it were the intent of Congress to require a formal demand for interest in order for the Government to have a lien for accrued interest as well as for the principal balance of an unpaid tax, it would then follow that the local Collector's Office would have to mail out revised Form 17's itemizing interest on each calendar day continuously from the date of assessment in order for the Government to have a lien right for the full amount of interest due it under the automatic provisions of Section 6601. We doubt that such was the intent of Congress, for it would conflict with the clear Congressional policy to give the United States priority rights for principal, interest and penalty from the date of assessment, such priority rights being the expressed public policy for the protection of the Federal Government and other contributing taxpayers, who are not delinquent.

Even if demand of interest be required, one Circuit Court has held that the demand can be subsequent and relate back. See *Matter of Fidelity Tube Corp.*, C.C.A. 3, 60-1 U.S.T.C. Sec. 9446, 278 F. 2d 776 holding that District Director's claims for taxes with the Referee in Bankruptcy relates back to the date of assessment against the bankrupt and satisfies the statutory requirement that there be a "demand" for payment in order for a lien to arise. So held with reference to claims where assessments made prior to bankruptcy but demands, if any, made afterwards, the opinion stating:

> "In view of the provisions of Section 3671 (now Section 6321) an inchoate lien seems to arise at the time of assessment which is perfected by a demand and when the demand is made the lien relates back to the

> date of assessment, in the case at bar to a time prior to bankruptcy."

See also *U. S. v. Allen*, 14 F. 263 (M.D. Tenn. 1882) and *In Re Baltimore Pearl Hominy Co.*, 5 F. 2d 553 (C.C.A. 4, 1925), the former recognizing the doctrine of "relation back" and the latter defining "demand".

Here the record below showed all the lien claims of the United States filed in the bankruptcy proceedings (E. 53, 187) and, additional, that the Bankrupt tried to pay this particular lien by a bad check received November 14, 1956 (E. 76, 77, 78). Applying the doctrine of "relation back", any requirement for demand was clearly satisfied. See also *U. S. v. Ettelson*, 159 F. 2d 193 (C.C.A. 7, 1947) holding that filing of the Government's claim in a Probate Court of Sufficient as demand.

The *Baltimore Pearl Hominy* case held that formal demand was dispensed with if the course of dealings between the Collector and the taxpayer showed that the taxpayer knew the extent of the Government's claim as evidenced by the tender of a check. Additional, the tender was held to constitute a waiver by conduct of the taxpayer's right to have demand made, which is a provision for his protection that he may waive.

Should it be held in this case that either that demand was not required or that such requirement was waived or was satisfied, there then arises the provocative question whether Section 6323 of Title 26, U.S.C.A., protects an unrecorded mortgagee, the enigma posed by the majority and dissenting opinions of this Court in the *Ball* case, supra.

We sincerely suggest that with the millions of taxpayers and billions in taxes involved in the operation of the Federal Government today, these are federal questions of

substance decided by a State Court but which have not yet been reached in this Court's chain of decision construing the tax lien principles of the United States, which this Court should now review and decide.

CONCLUSION

For the foregoing reasons, we urge this Court to grant the writ of certiorari requested by the petitioner.

Respectfully submitted,

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APPENDIX A

STATUTES INVOLVED

Title 26, Sec. 6321. *Lien for Taxes*—

"If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person."

Title 26, Sec. 6322. *Period of Lien*—

"Unless another date is specifically fixed by law, the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed is satisfied or becomes unenforceable by reason of lapse of time."

Title 26, Sec. 6323. *Validity against mortgagees, pledgees, purchasers, and judgment creditors*—

"(a) Invalidity of lien without notice. — Except as otherwise provided in subsection (c), the lien imposed by section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the Secretary or his delegate—

(1) Under state or territorial laws. — In the office designated by the law of the State or Territory in which the property subject to the lien is situated, whenever the State or Territory has by law designated an office within the State or Territory for the filing of such notice; or

* * * * * *

Title 26, Sec. 6601. *Interest on underpayment, nonpayment, or extensions of time for payment, of tax.*

(a) General rule. — If any amount of tax imposed by this title (whether required to be shown on a return, or to be paid by stamp or by some other method) is not paid

on or before the last date prescribed for payment, interest on such amount at the rate of 6 percent per annum shall be paid for the period from such last date to the date paid.

* * * * * *

(f) Applicable rules. — Except as otherwise provided in this title—

(1) Interest treated as tax. — Interest prescribed under this section on any tax shall be paid upon notice and demand, and shall be assessed, collected, and paid in the same manner as taxes. Any reference in this title (except subchapter B of chapter 63, relating to deficiency procedures) to any tax imposed by this title shall be deemed also to refer to interest imposed by this section on such tax.

(2) No interest on interest. — No interest under this section shall be imposed on the interest provided by this section.

(3) Interest on penalities, additional amounts, or additions to the tax. — Interest shall be imposed under subsection (a) in respect of any assessable penalty, additional amount, or addition to the tax only if such assessable penalty, additional amount, or addition to the tax is not paid within 10 days from the date of notice and demand therefor, and in such case interest shall be imposed only for the period from the date of the notice and demand to the date of payment.

(4) Payments made within 10 days after notice and demand. — If notice and demand is made for payment of any amount, and if such amount is paid within 10 days after the date of such notice and demand, interest under this section on the amount so paid shall not be imposed for the period after the date of such notice and demand.

* * * * * *

Title 11, Sec. 70. *Title to property.*

* * *

(e) (1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this title which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this title, shall be null and void as against the trustee of such debtor.

(2) All property of the debtor affected by any such transfer shall be and remain a part of his assets and estate, discharged and released from such transfer and shall pass to, and every such transfer or obligation shall be avoided by, the trustee for the benefit of the estate: Provided, however, That the court may on due notice order such transfer or obligation to be preserved for the benefit of the estate and in such event the trustee shall succeed to and may enforce the rights of such transferee or obligee. The trustee shall reclaim and recover such property or collect its value from and avoid such transfer or obligation against whoever may hold or have received it, except a person as to whom the transfer or obligation specified in paragraph (1) of this subdivision is valid under applicable Federal or State laws.

(3) For the purpose of such recovery or of the avoidance of such transfer or obligation, where plenary proceedings are necessary, any State court which would have had jurisdiction if bankruptcy had not intervened and any court of bankruptcy shall have concurrent jurisdiction.

APPENDIX B

OPINION OF COURT OF APPEALS OF MARYLAND

(Filed March 9, 1961)

No. 140, September Term, 1960

Lewin Wethered, Trustee of the Estate of John B. Gaither, Jr., Inc., Bankrupt,

v.

Alban Tractor Co., Inc., Herbert L. Wynne, Trustee and Plaza Corporation.

Before: Henderson, Hammond, Prescott, Horney and Sybert, J.

Opinion by Hammond, J.

A bankruptcy trustee, seeking to capture for the estate the proceeds of sale on foreclosure of an unrecorded chattel mortgage given by the bankrupt, contends on appeal from a decree rejecting his claim that he stands in the shoes of lien creditors who could have set aside the chattel mortgage and, therefore, that the mortgage and its foreclosure were ineffective as to him.

The problems the case presents arise out of the financing procedures of the bankrupt, a corporation known as John B. Gaither, Jr., Inc., and are not entirely new to this Court. Two aspects of them have been before us on prior appeals. In *O'Toole Tire Company v. John B. Gaither, Jr., Inc.*, 216 Md. 54, it was held that Gaither's legal corporate residence was Baltimore County, not Baltimore City as was claimed. In *Plaza Corporation v. Alban Tractor Co., Inc.*, 219 Md. 570 (hereinafter referred to as "the *Plaza-Alban* case"), the holding was that as between Plaza's and Alban's respective mortgages, neither of which was recorded in Baltimore County, Plaza's was superior as having been first executed.

In October 1954 Gaither purchased from Alban various construction and contracting machines on a conditional contract of sale in the amount of some $200,000. On December 1, 1954, Gaither gave Plaza a mortgage covering some of the chattels covered by Alban's conditional contract, other chattels and real estate. The mortgage was sent to the clerk of the Circuit Court for Baltimore County, who recorded and indexed it in the Land Records but did not list it in the chattel index. In May 1955 Alban sold Gaither $119,000 worth of additional machinery, paid off the bank to which it had assigned the conditional sales contract of 1954 and took a mortgage from Gaither which covered the newly purchased machinery and that which had been in the conditional contract. This mortgage was promptly recorded in Baltimore City but also has never been recorded in Baltimore County.

Gaither defaulted in the payment of the 1955 mortgage to Alban, which filed a petition seeking foreclosure in the Circuit Court No. 2 of Baltimore City on November 5, 1956. That same day a decree was passed, appointing the attorney named in the mortgage as Alban's agent, the trustee to make sale. On the two following days Alban repossessed the various pieces of machinery and equipment covered by its mortgage, all of which apparently were then in Baltimore City, and stored them in its yard in the City, open to inspection prior to the sale which was duly and widely advertised to take place there on December 1, 1956. At the sale $67,200 was realized on the chattels named in both the Alban and Plaza mortgages, and $81,300 on those covered only by the Alban mortgage from purchasers who paid cash in full and took away their purchases. Plaza filed exceptions to ratification, and on June 6, 1957, the sale was ratified under a stipulation that the respective rights of Plaza and Alban in the chattels would carry over to the proceeds of sale. Later, the chancellor dismissed the exceptions, holding that Gaither's principal office was in Baltimore City and, therefore, Alban's mortgage had been properly recorded there, and Plaza's mortgage was unrecorded.

On Plaza's appeal in the *Plaza-Alban* case, we reaffirmed the *O'Toole* holding that Gaither's legal residence was Baltimore County and held that both mortgages were unrecorded in that jurisdiction, the rights of the holders of unrecorded mortgages is determined by priority of execution and Alban did not come under the protection given a subsequent mortgagee against a prior unrecorded mortgage by Code (1957), Art. 21, Sec. 41, because that section contemplates that a subsequent mortgage must be recorded if it is to prevail. Thus Plaza's mortgage, executed in 1954, was held to come ahead of Alban's executed in 1955.

On May 12, 1958, Gaither was adjudicated an involuntary bankrupt. The trustee in bankruptcy sought to intervene in Plaza-Alban's appeal to this Court and was denied leave, but granted the right to file a brief as amicus curiae. His brief challenged the jurisdiction of the Baltimore City equity court to foreclose the Alban mortgage.

After the reversal in the *Plaza-Alban* case, the trustee in bankruptcy filed pleadings in the foreclosure proceedings, claiming (a) the court lacked jurisdiction to foreclose Alban's mortgage; (b) its mortgage was void and did not pass or transfer any property as against the trustee because it was not recorded in the proper place; (c) the United States has claims against Gaither "provable under the Bankruptcy Act," underlying a tax lien on all of Gaither's property and property rights, which had been assessed on August 22, 1956, several months before the mortgage foreclosure (and on which notice of tax lien had been filed in Baltimore City on December 27, 1956, and in Baltimore County the next day) and four other similar assessments made in 1957 and 1958 (as to which notices of lien also were duly filed soon after assessment);[1] (d) the State of Maryland and Baltimore County have claims for various kinds of taxes provable in bankruptcy which were "quasi-liens;" (e) the Federal and State and local liens

[1] The appellant, the trustee in bankruptcy, bases his right to prevail primarily on the 1956 assessment of $305.06 and the conclusions we reach as to that makes the other four later assessments of no significance in the determination of the case.

were superior to the mortgage; and (f) under various sections of the Bankruptcy Act the mortgage was null and void as against the trustee, the chattels therein described remained Gaither's property and the trustee is entitled to be paid the proceeds of sale for the benefit of unsecured creditors.

The trustee's main reliance is on section 70(e) of the Bankruptcy Act (11 U.S.C.A. Sections 110(e) (1), (2) (1953)). His argument is that liens on all Gaither's property and rights in property were created by Sections 6321, 6322 and 6323 of the Internal Revenue Code of 1954 (26 U.S.C.A. Secs. 6321, 6322 and 6323 (1955)), as to the $305.06 Federal assessment of August 22, 1956, and as to the State and County tax claims, by virtue of which the Federal Government or the State or County could have set aside the unrecorded mortgage, and he, under the express provisions of Sec. 70(e) is put in the shoes of the lienors.

Section 70(e) provides: "(1) A transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this title which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this title, shall be null and void as against the trustee of such debtor." "(2) * * * The trustee shall reclaim and recover such property or collect its value from and avoid such transfer or obligation against whoever may hold or have received it, except a person as to whom the transfer or obligation specified in paragraph (1) of this subdivision is valid under applicable Federal or State laws."

Code (1957), Art. 21, Sec. 41, as amended in 1949, provides that "No personal property * * * whereof the vendor, mortgagor, or donor shall remain in possession, shall pass, alter or change, or any property therein be transferred to any purchaser, mortgagee or donee, as against subsequent purchasers, mortgagees, incumbrancers, landlords with liens, pledgees, receivers, and creditors who acquired a lien by judicial proceedings on such personal property, unless

by bill of sale or mortgage acknowledged and recorded as herein provided * * *."

It becomes apparent that the correctness of the trustee's contention turns on whether the Federal Government or the State or Baltimore County came within one of the categories entitled to prevail over an unrecorded mortgage by Sec. 41 of Art. 21. *Tatelbaum v. National Store Fixture Sales Co.*, 196 Md. 599, 604; the *Plaza-Alban* case. If it does apply, the effect of Section 70(e) is far-reaching and startling. For example, if the Federal Government had a lien for $305.06 which became superior to that created by Alban's mortgage, in actuality Alban would have paid the $305.06 so as to protect its lien for several hundred thousand dollars. However, if the bankruptcy trustee is entitled to step into the shoes of a superior lienor or encumbrancer, he can nullify the mortgage entirely, obtain $148,000 because the bankrupt owed $305.06, and relegate the mortgagees to the status of unsecured creditors.[2] This result was approved in *Moore v. Bay*, 284 U.S. 4, 76 L. Ed. 133, and the holding of that case was incorporated into Sec. 70(e) by the Chandler Act. If the trustee is right, unsecured creditors of Gaither, as to whom the mortgage would be valid and superior under Maryland law, would share in bankruptcy in the proceeds of sale of the mortgaged chattels. See MacLachlan, *The Impact of Bankruptcy on Secured Transactions*, 60 Col. L. Rev. 593, 599, 604, 606.

We think neither the State, Baltimore County nor the United States had a lien on any chattel of Gaither covered by the mortgage before it was sold to a bona fide purchaser and that the day of the sale marked the close of the period in which any creditor could acquire a lien upon Gaither's property or right of property in the mortgaged chattels. There was no State or local lien because the Maryland statutes neither create a lien for unpaid taxes other than those on real estate nor purport to do so, and

[2] Plaza would not be entirely displeased by this, as its brief and oral argument admit, since its claim as an unsecured creditor would be approximately 75% of all unsecured claims.

this Court has held that no such lien arises short of execution or distraint; and there was no federal lien because that government made no demand upon Gaither for the payment of any tax (a mandatory, statutory prerequisite to the creation of such a lien) at a time when Gaither had any property rights of property to which a lien could attach.

The Supreme Court in *Aquilino v. United States*, 363 U.S. 509, 513, 4 L. Ed. 2d 1365, 1368, and *United States v. Durham Lumber Co.*, 363 U.S. 522, 526, 4 L. Ed. 2d 1371, 1374, delineated with definiteness the rules determining the effect of the statutes creating federal tax liens. They said that the issue is whether, and to what extent, the taxpayer had property or rights in property to which the tax lien could attach. The lien sections, the Court reiterated, create no property rights but merely attach consequences, federally defined, to rights created by State law, citing *United States v. Bess*, 357 U.S. 51, 55, 2 L. Ed. 2d 1135, 1140. State law controls in determining the nature and extent of the legal interest which the taxpayer had in the property sought to be reached by the lien but once the lien has attached to the taxpayer's state created interest, federal law determines the priority of competing liens asserted against his property or rights therein.

The claims of the State were for income and sales taxes, contributions to Maryland unemployment compensation and premiums for compensation insurance. Baltimore County's claim was for tangible personal property taxes for 1955 and 1956. Neither the State nor the County was a lienor or incumbrancer. The statutes do no more than establish a priority of payment for unpaid taxes, other than those upon real estate, upon a sale of the property of a debtor by any ministerial officer "under judicial process or otherwise." Code (1957), Art. 81, Sec. 202. This does not establish a lien. *Thompson v. Henderson*, 155 Md. 665; *In re Beardsley*, 38 F. Supp. 799, 804. See also *Rouse v. Archer*, 149 Md. 470. There is a lien for such taxes only after levy and distraint. *Union Trust Co. v. Belvedere Building Co.*, 105 Md. 507.

The critical claim of the Federal government was for taxes withheld from income and Federal Insurance Contribution Act taxes. The trustee in bankruptcy produced evidence below that Gaither's return for the second quarter of 1956, which was due on or before July 31, 1956, was not received until August 3 (although Gaither's auditor testified it was mailed on July 31, which would have made it timely filed), and that no remittance for the $5,705.32 shown to be due accompanied the return. On August 14, Gaither paid the $5,705.32 which should have been paid by July 31. Nevertheless, on August 22 the United States entered an assessment against Gaither for $5,705.32, plus penalty of $285.27 for late filing and, apparently, interest from July 31 to August 22 in the amount of $19.79 (since payment was made on August 14 the interest due actually would have been some $13.00). On August 22, Gaither was sent Form 17 "Statement of Tax Due on Employer's Quarterly Federal Tax Return (income tax withheld for wages and FICA taxes)." It showed "Assessment (1)" of $8,978.05 and "Pen." $285.27, or a total of $9,263.32 and a credit of $3,272.73 (which had been paid June 15, 1956), leaving a "Balance due" shown as $5,990.59. The credit allowed should have been increased by the $5,705.32 paid August 14, 1956, which would have left a balance due of $285.27.

On Form 17 the legend "(1)" following the heading "Assessment" referred to a note reading as follows: "(1) 'P' denotes penalty, 'I' denotes interest." No interest was shown or demanded on the form sent Gaither. A recital on the form said: "According to our records the tax was not paid in full. You will be saved inconvenience and *further expense* by making payment of the *'Balance due'* within 10 days of the date of this notice." (Emphasis supplied.) The only "expense" shown on the form was the penalty and the "Balance due" included the penalty but no interest. The trustee's witness, an attorney who was chief of the special procedure section of the Internal Revenue Service of the United States at Baltimore, testified that the usual practice was not to assess or collect interest if the amount demanded was paid in ten days and, referring to the recital that "further expense" would be

avoided by payment within ten days, said: "That is the statement contained in form 17, notice of payment." He also testified that "Apparently the form 17, notice of demand, has omitted to claim assessed interest of $19.79."

The notice of lien filed in the Superior Court of Baltimore on December 27, 1956, and the Circuit Court for Baltimore County December 28, 1956, recited (substantially in the language of the statutes) that pursuant to Sections 6321, 6322 and 6323 of the Internal Revenue Code of 1954, notice is given that there have been assessed against the named taxpayer "taxes (including interest and penalties) which after demand for payment thereof remain unpaid, and that * * * the amount of said taxes * * * is a lien in favor of the United States upon all property and rights to property belonging to said taxpayer." The amount of the assessment is shown only as $305.06.

It is plain from the record that the Federal government has no claim provable in bankruptcy which became a lien on the mortgaged chattels. The trustee concedes that the penalty assessed is not a provable claim. Sec. 57, Sub. j of the Bankruptcy Act (11 U.S.C.A., Sec. 93, Sub. j (1960 Supp.)) so specifies as to a debt owed the United States or any State or subdivision thereof as a penalty and the Court of Appeals for the Fourth Circuit held in *United States v. Harrington*, 269 F. 2d 719, 725, that a penalty remains unprovable even though it is secured by a perfected lien. Although there are contrary holdings by other lower Federal Courts, the Supreme Court by its decision that the allowability of a claim underlying a judgment lien on a judgment against a bankrupt could be inquired into (*Pepper v. Litton*, 308 U.S. 295, 84 L. Ed. 281), and its later statement that the Court "may also adjudicate questions pertaining to the amount of a tax claim secured by a lien * * *. There is, for example, the question whether the amount of the claim has been swollen by the inclusion of a forbidden penalty and thus to that extent does not meet the bankruptcy requirements for proof and allowance of claims." (*Gardner v. State of New Jersey*, 329

U.S. 565, 580, 91 L. Ed. 504, 518), has indicated that Judges Sobeloff, Haynsworth and Barksdale were right in their holding in *Harrington*.

The interest included in the amount of $305.06 specified in the notice of lien duly recorded is provable in bankruptcy but no lien ever arose as to it because it was never demanded to be paid. Section 6321 creates a lien only if a person owing a tax "neglects or refuses to pay the same after demand." The trustee's own witnesses and exhibits demonstrated there had never been a demand for the interest. (Indeed, the impression created by Form 17 would be that interest was not being assessed.) In such situation the Courts have held that no lien arises and that the mere recital in the notice of lien filed in the appropriate land or chattel records that it is for taxes "which after demand for payment thereof remain unpaid" lacks the necessary specificity to constitute the required statutory demand. In *United States v. Pacific Railroad Co.*, 27 Fed. Cas. 399, 401 (No. 15,984) (C.C.E.D. Mo.), the Court said that to create the lien all requisite prescribed steps must be "pursued strictly" and that "One of the evidences of that must be a demand for the payment of taxes. Another one, it seems to me, ought to be a demand for the specific amount to be paid." The Court, in the case of *In re Crockett*, 150 F. Supp. 352, 354 (D.C.N.D. Cal.), said that by the plain wording of the statute "the lien does not attach unless and until the delinquent taxpayer 'neglects or refuses to pay the same after demand'" and that it was incumbent on the United States to show that the statutory prerequisites have been fulfilled before it can be treated as a lien creditor. The District Court for the District of Massachusetts made the same holding in *Sherman B. Ruth, Inc. v. O. S. V. The Marie and Winifred*, 150 F. Supp. 630, 632, and added: "The mere formal reference in the notice of tax lien to 'taxes (including interest and penalties) which after demand for payment thereof remain unpaid' is not a sufficient demand for payment of the tax to provide basis for a tax lien." *Cattani v. Korsan* (Super. Ct. N.J.), 103 A. 2d 51, held the United States must prove that demand was made if its lien is to exist and the statement in the notice of lien duly

filed is not sufficient to satisfy the mandatory requirement of demand. See also *United States v. Allen* (C.C.M.D. Tenn.), 14 F. 263; *In re Holdsworth* (D.C.N.J.), 113 F. Supp. 878; *Goldstein v. Bankers Commercial Corp.* (D.C. S.D.N.Y.), 152 F. Supp. 856, 859, aff'd 257 F. 2d 48; *United States v. Kentucky* (Ky.), 288 S.W. 2d 664. Cf. *United States v. Brechtel* (C.C.A., 8th), 90 F. 2d 516.

It is conceded that the chattel mortgage given by Gaither to Alban was made in the ordinary course of business in entire good faith and for full value. It was valid and enforceable in a court of equity as a lien not only between Gaither and Alban but as to every one else who was not within one of the seven protected classes under Code (1957), Art. 21, Sec. 41 — that is as against all but a subsequent purchaser, mortgagee, incumbrancer, landlord with lien, pledgee, receiver or a creditor with a lien acquired by judicial proceedings. *Plaza-Alban* case (588-589 of 219 Md.). See also *Textor v. Orr*, 86 Md. 392; *Goldsborough v. Tinsley*, 138 Md. 411, 419; *Tatelbaum v. National Store Fixture Sales Co.*, 196 Md. 599. A court of equity has inherent power to enforce the lien of a mortgage whether it be recorded or unrecorded. *Jackson v. County Trust Co.*, 176 Md. 505; *Goldsborough v. Tinsley, supra*; Restatement, *Restitution*, Sec. 161, page 650 (1937); *Sanford v. Boland* (N.Y.), 40 N.E. 2d 239. The opinion in the *Plaza-Alban* case, 577, pointed out that "Foreclosure of mortagages after default has long been peculiarly within a court of equity's jurisdictional powers" and that the provisions of Code (1957), Art. 66, Sec. 6, under which Alban proceeded, simply provides "an expeditious and economical summary modal procedure for the exercise of an ordinary jurisdiction." See Jones, *Chattel Mortgages*, Sec. 776 (6th Ed.). It was implicit in the holding of the *Plaza-Alban* case that the court below had jurisdiction to, and effectively did, foreclose Alban's mortgage. We confirm explicitly here what was there implicit. The chattels being sold were in Baltimore City, and the parties were before a court which had inherent power to order and consummate the sales that were made in the enforcement of the mortgage security title. All the parties in interest were repre-

sented in the prior appeal; Gaither was a defendant and the trustee in bankruptcy filed a brief as amicus curiae. The *Plaza-Alban* decision established that the Alban mortgage was valid and the sale under foreclosure effective to pass title to the chattels sold. The trustee has not shown that any lien in favor of the United States came into being before all property or rights to property in the mortgaged chattels passed from Gaither, its debtor, and therefore it was not a lienor or incumbrancer as to those chattels. The trustee in bankruptcy has no lien shoes in which to step so as to set aside the Gaither mortgage to Alban.

If it be assumed that the United States acquired a lien on December 27, 1956, when it filed the notice of lien, the trustee's position under Section 70(e) of the Bankruptcy Act would not seem to have been improved. The Federal lien was a general lien inferior to the claim of a purchaser until filed under the federal statute, Sec. 6323(a) of the Internal Revenue Code ("The lien imposed by Section 6321 shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed * * *."). As to all against whom it was effective, it would have been, from the time it arose, a lien comparable to that of a judgment creditor on the real property of his debtor. It was held in *Union Trust Co. v. Biggs*, 153 Md. 50, 56, that a judgment obtained after the day of sale of real estate in a foreclosure proceeding and before the day of confirmation of the sale by the court did not become a lien on the real estate. It was pointed out that legal title does not vest in the purchaser at a foreclosure sale until the price is paid and a deed is delivered but that the deed is effective, not merely from the day of its execution, but vests the property in the purchaser from the day of sale. The Court said: "The day of sale, therefore, marked the close of the period in which any creditor could acquire a lien upon the mortgagor's interest in the mortgaged land or equity of redemption by simply obtaining a judgment against the mortgagor, since a judgment lien upon real estate or an equitable interest in land only exists because it gives the judgment creditor the right to make his debt out of the land or equitable interest in land of the

judgment debtor, with the correlative liability of such property of the debtor to be sold by way of execution for that purpose."

In the case before us the chattels were sold for cash in full and delivered to bona fide purchasers on December 1, 1956, twenty-six days before the first notice of lien for $305.06 was filed by the United States. Payment in full of the purchase price and delivery of the chattel to the buyer generally is all that is required to vest full legal title in the purchaser. Certainly Gaither, which had explicitly authorized the sale in its contract with Alban, embodied in the chattel mortgage, could not complain that its rights of property in the chattels ended when bona fide purchasers paid for them and took them away, and its creditors without liens are in no better position. By the terms of the chattel mortgage (which appears in the record of the *Plaza-Alban* appeal in this Court) Alban became entitled to possession upon default and Gaither authorized Alban or its named attorney or agent, in such case, "to sell the hereby mortgaged property." Gaither further agreed that after default, unless legal tender were made of the principal, costs, expenses and commissions before the advertised day of sale, the sale could be proceeded with. This could be construed as an agreement that the right to redeem ceased as of the time of sale.

In Maryland where a mortgage passes legal title to the mortgagee, the right to possession follows the title and, in the absence of agreement, the mortgagee is entitled to hold the mortgaged chattels. In practice, the mortgage in terms usually gives the mortgagor the right to retain possession until default. Immediately upon default the mortgagee has the full right to take the chattels. *Shorter v. Dail*, 122 Md. 101, 105. After default the mortgagee may maintain trover as to the mortgaged chattels, *Burton v. Jennings*, 158 Md. 254, 257, or sue one who has converted them in assumpsit for the sales price, *Leighton v. Preston*, 9 Gill 201, 203. At the old common law the title of the mortgagee became absolute upon default without foreclosure and there was no right to redeem. Now an opportunity to redeem is required. *Dungan v. Mutual Benefit*

Life Ins. Co., 46 Md. 469, 491. That case held that a life insurance policy could be mortgaged and that after default and due notice to the mortgagor to redeem, the mortgagee may "proceed to sell, without the trouble and delay of bringing a bill to foreclose; and in such case the title, if the sale be *bona fide* made, will vest absolutely in the vendee."

We think that Gaither's right to redeem ceased with the fully advertised and fairly held sale to bona fide purchasers who paid cash in full. As the Court of Appeals for the Fourth Circuit said in *United States v. Durham Lumber Company*, 257 F. 2d 570, 574, affirmed 363 U.S. 522, 4 L. Ed. 2d 1371: "If the delinquent taxpayer has no right under state law, there is nothing upon which the tax lien may attach." The sale did not produce enough to satisfy the mortgage debt so Gaither and his creditors had no rights as to the cash in the foreclosure trustee's hands. The Supreme Court in *United States v. Brosnan*, 363 U.S. 237, 4 L. Ed. 2d 1192, held that sales of property under State liens superior to Federal tax liens, which were valid to pass title, extinguished the Federal liens.

We need not determine whether the taking of possession after default, the foreclosure decree and the advertising of the sale were the equivalent of recording so as to mark the point in time when a lien of a creditor of Gaither's could attach ahead of the lien of Alban's mortgage. There is authority that they would have been such an equivalent. *Kratzmer v. Detroit Lumber Co.* (Mich.), 161 N.W. 817. See also *Goggin v. Division of Labor Law Enforcement*, 336 U.S. 118, 93 L. Ed. 543; *United States v. Sands* (2nd Cir.), 174 F. 2d 384; *Brust v. Sturr* (2nd Cir.), 237 F. 2d 135; *Davis v. City of New York* (C.C.A. 2nd), 119 F. 2d 559. Cf. *United States v. Gilbert Associates*, 345 U.S. 361, 97 L. Ed. 1071, and *Lochner v. Moreland* (4th Cir.), 192 F. 2d 985, 987.

Nor do we reach the question whether when Section 6323 says the Federal lien shall not be valid as against "any mortgagee" until notice of the lien has been filed, it includes a mortgagee under an unrecorded mortgage;

that is, whether a non-statutory contractual lien must be choate and perfected to prevail. The Supreme Court has never given an explicit answer. In *United States v. Ball Construction Co.*, 355 U.S. 587, 594, 2 L. Ed. 2d 510, 515, an assignment by a sub-contractor to a surety company was involved. The District Court and the Court of Appeals held the assignment to be a chattel mortgage under State law and, even though unrecorded, to be superior to the Federal tax lien on the property of the sub-contractor. Five Justices of the Supreme Court reversed in a four-line per curiam, saying that since the "instrument" was inchoate the statute preferring named claimants did not apply. The majority did not characterize the assignment as a mortgage and the citations relied on were cases involving non-contractual liens. It would seem to be more likely than not (although not clear) that the majority were of the opinion the assignment was not a mortgage within the meaning of the federal statute preferring mortgages to unfiled Federal tax liens.

Justices Whittaker, Douglas, Burton and Harlan dissented on the view that the assignment was in legal effect a mortgage, and since it antedated the filing of the Federal lien it was superior to it. Justice Whittaker said for the dissenters that the unrecorded mortgage was specific, choate and valid between the parties as of its date and, "inasmuch as it antedated the filing of the federal tax liens it was expressly made superior to those liens by the terms of §3672(a) Section 6323 I.R.C."

The lower Federal Courts and the commentators have not agreed on the meaning to be given the *Ball* case. Typical is the reaction of the appellate Judges of the Fourth Circuit, expressed in *United States v. Bond*, 279 F. 2d 837, certiorari denied, 5 L. Ed. 2d 189. Judges Boreman and Sobeloff read the *Ball* case as confirming that only a technically choate and perfected State lien will prevail over a Federal tax lien and as showing that this test, first made applicable in insolvency cases and then in statutory lien cases, has now been extended to non-statutory contractual

lien situations. Judge Haynsworth disagreed, feeling that the *Ball* case did no more than hold the assignment was not a mortgage.

Other lower court Federal Judges generally seem to have inclined to Judge Haynsworth's views.

In *United States v. Eagle* (D.C.E.D.S.C. 1959), 59-2 U.S.T.C. Paragraph 9656, the United States was held not to be a protected creditor in respect of its tax lien vis a vis a State statute, preferring those who deal with and trust the debtor after the execution of the unrecorded mortgage. Reliance was put on *United States v. Anders Contracting Co.* (D.C.W.D.S.C.), 111 Supp. 700, which held that a conditional sales contract, classed as a chattel mortgage under South Carolina law, which was valid between the parties need not be recorded to be effective against the Government's tax lien. Judge Wyche concluded that the *Ball* case held that the assignment was not a mortgage and that the opinion of the minority gave support to the conclusion he had reached in *Anders* and in *Eagle*. The same conclusion has been reached by District Judges in *Gauvey v. Basin Rig and Trucking, Inc.* (D.C.N.), 185 F. Supp. 374, 377 (1960), and *Diamond T. Motor Co. v. Allen, District Director*, 60-2 U.S.T.C. Paragraph 9557 (D. Ct. Colo.). The Government did not appeal *Anders* or *Eagle* and has announced it will not appeal *Diamond T.* Cf. *United States v. Torres* (D.C. Md. by Soper, J.), 291 F. 138, 141, a pre-*Ball* case.

There are other pre-*Ball* cases holding that an unrecorded mortgage will not prevail over a Federal tax lien. Some are referred to in the *Plaza-Alban* case at page 592 of 219 Md. Generally they are applying laws of states which make the unrecorded mortgage void rather than ineffective as to specified creditors. The answer to whether the unrecorded mortgage prevails over the Government tax lien can be finally and definitely given only by the Supreme Court. An able and interesting discussion of the cases and the problem is to be found in "*Applicability of the 'General and Unperfected Lien' Doctrine to Contractual Liens*," 43 Minn. L. Rev. 755.

We turn to the other Sections of the Bankruptcy Act relied on by the trustee in bankruptcy.

Section 70(c) (11 U.S.C.A. Sec. 110, c), unlike Section 70(e) which requires an actual lien creditor, gives the trustee the rights of an hypothetical or ideal lien creditor upon property in which the bankrupt has an interest or as to which he may be the ostensible owner. In *Lewis v. Manufacturers Bank*, U.S. , 5 L. Ed. 2d 323, 326, decided after the decision in this case below and shortly before argument in this Court, the Supreme Court held that under Section 70(c): "The rights of creditors — whether they are existing or hypothetical — to which the trustee succeeds are to be ascertained as of 'the date of bankruptcy,' not at an anterior point of time. That is to say, the trustee acquires the status of a creditor as of the time when the petition of bankruptcy is filed."

In the case before us the trustee acquired his status as a creditor under Sec. 70(c) sixteen months after the chattels had been sold and ten months after the sale had been finally ratified and confirmed. As of bankruptcy there was no property as to which a creditor (and, so, the trustee) could acquire a lien. As the chancellor below, artfully anticipating the *Lewis* decision, aptly and accurately observed: "The Act creates a hypothetical creditor even though no such creditor actually exists, but it has not undertaken hypothetically or otherwise to create property where none exists." The trustee has no right under Section 70(c).

Under Section 70(a) (11 U.S.C.A. Sec. 110, a), the trustee is vested with the title of the Bankrupt, as of the date of the filing of the petition, to "(5) property * * * which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him * * *." When the petition was filed Gaither did not own the mortgaged chattels and had no interest in them which it could have transferred or which might have been levied upon or sold. Bankruptcy came many months too late for this.

Section 60 of the Bankruptcy Act (11 U.S.C.A. Sec. 96) deals with preferential transfers of the debtor, while insolvent, to or for the benefit of a creditor of an antecedent debt. Sub-section (a)(2) provides that if such a transfer is not so perfected prior to the filing of the petition in bankruptcy that "no subsequent lien upon such property obtainable by legal or equitable proceedings on a simple contract could become superior to the rights of the transferee," the transfer shall be deemed to have been made immediately before the filing of the petition.

The chancellor found, with substantial reason, we think, that there was no proof of Gaither's insolvency before bankruptcy. The petition was filed in April 1958. At that time the transfer of Gaither's property to bona fide purchasers for value had been an accomplished fact, fully perfected for some ten months. Section 60 is of no avail to the trustee.

The dismissal below of the trustee's petition was proper.

DECREE AFFIRMED, WITH COSTS.

AUG 10 1961

JAMES R. BROWNING, Clerk

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 225

LEWIN WETHERED, TRUSTEE OF THE ESTATE OF JOHN B. GAITHER, JR., INC., BANKRUPT,
Petitioner,

v.

ALBAN TRACTOR COMPANY, INC., HERBERT L. WYNNE, TRUSTEE, AND PLAZA CORPORATION,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

BRIEF OF ALBAN TRACTOR COMPANY, INC. AND HERBERT L. WYNNE, TRUSTEE (TWO OF THE RESPONDENTS HEREIN) IN OPPOSITION

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The Daily Record Co., Baltimore 3, Md.

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JURISDICTION

The Trustee in Bankruptcy seeks the issuance of a Writ of Certiorari on the ground that the Court of Appeals of Maryland has decided Federal Questions of Substance not heretofore determined by this Court (Petition — 6); concluding (8*) with the suggestion that the decision turned

* Page references, unless otherwise noted, are to the Petition for a Writ.

upon Federal Questions of Substance "not yet * * * reached in this Court's chain of decision construing" certain tax principles.

Doubtless it is noteworthy that the Treasury Department, though its representatives, in the presence of Government counsel, testified in the trial Court and were aware of the decisions, does not join with the Trustee in Bankruptcy in advancing the contention presented here to this Court.

These Respondents contend that this case does not relate to a Federal question of substance; moreover, that the Maryland Court of Appeals correctly decided that question (that interest, as well as the principal amount of the tax itself, must be demanded to be paid — by the firm language of the tax Statute, as well as by long administrative practice — in order that the item of interest, in addition to becoming a *claim*, may also become a *lien*).

We contend also that the final decision below classicly turned upon State law — the nature of property rights or interests in property, and the effect of the recording statutes of Maryland — and hence apart from the correctness of the decision on the demand of interest point, basically involved state determinations of propositions governed by State law.

CONCERNING THE FACTS

The material facts involved in the decision below appears on Pages 14 through 17, and again on Pages 20 and 21, and finally, on Page 25 of the State Court Opinion, as reproduced at those pages in the Petitioner's Appendix B, and will not therefore be separately restated.

QUESTIONS PRESENTED

Of the Three Questions which the Petitioner propounds for consideration by this Court, he concedes that the Second was not expressly decided, and that the Third was expressly left open by the State Court. Yet, the Court of Appeals *quite clearly indicated a decision* on still another State law controlled point, i.e., the taking of possession, after default, of the mortgaged chattels, as the "*equivalent of recording*" of the mortgage, (Petitioner's App. B-26), which would render it unnecessary to pass upon any of the questions posed by the Petitioner. The State Court's determination on this "equivalent of recording" question, a conclusion pivoting solely upon State law, renders it unnecessary to consider Petitioner's Third Question at all and his contention thereon becomes altogether moot in this case. Furthermore, his Third Question continues to assume, as a fact, that the chattel mortgage is to be regarded as still unrecorded, notwithstanding the State Court's "equivalent of recording" observations — and despite its valid foreclosure.

Since, as the Appellate Court noted, (1) possession of the chattels is treated as the equivalent of recording, (2) the tax lien was admittedly not recorded until (a) after such recording equivalent had occurred and also (b) after public auction sale, for cash, to third party bona fide purchasers had been completed, (3) Bankruptcy did not occur until some sixteen months after *such recording equivalent and sale*, we contend either that Petitioner's Third Question has been disposed of on State grounds (equivalent of recording) or that it is otherwise unnecessary of answer here.

In that posture of the case Petitioner's First Question is entirely moot also and, disregarding the correctness of the

Court's decision on that point, an ineffectual subsidiary of the larger determination so finally made or indicated by the Appellate Court with respect to an issue alone controlled by State law.

Correctly stating the spheres of influence, as between Federal and State law, the Maryland Court of Appeals (Petitioner's App. B—19), soundly applying the controlling State law, determined, solely on State grounds, that all property and rights to property in the mortgaged chattels had, prior to the recording of the tax lien — which by Sec. 6322 of Title 26 of U.S.C.A. is required in order to give it any validity against a mortgagee or purchaser — been effectively passed from the chattel mortgagor to such purchasers and that the Trustee in Bankruptcy, who first came into being some sixteen months later, was not a lienor or encumbrancer within the meaning of the Maryland Statute on recording. This application of the Maryland law with regard to local property interests — and the determination of such property interests is exclusively the function of the State Court — disposed of the claim of the Trustee upon principles of State law.

Petitioner's application for a Writ in this case does not and cannot reach that proposition — turning, as it did, entirely upon Maryland law.

Mention should be made of the further fact that the State Court did not find it necessary in this case to rule upon another point involved in the case and argued by the parties to that Appeal. The Maryland Statute on recording (which we set forth in the Appendix to this Brief) is, as frequently is found to be the case in the various States, the product of long development, molded by numerous State decisions and legislative modifications. It

expressly makes unrecorded chattel mortgages *valid and enforceable* against all *except certain specifically designated classes*, including "subsequent purchasers, mortgagees, incumbrancers, landlords with liens, pledgees, receivers, and creditors who acquired a lien by judicial proceedings on such personal property". The Court below (Appendix B — 18 and 23) discussed this Statute and its coverage and consequences.

It was argued before the State Court, following State precedents, that even with regard to these designated classes, an unrecorded chattel mortgage was valid and enforceable unless *credit had been extended* by one of such classes in reliance upon possession of the chattel by the debtor.

Maryland decisions, describing the State's recording statutes as being intended to protect "trusting" creditors specifically dealing with such chattels (as, for example, a subsequent mortgagee, pledgee, purchaser), were pointed to as standing for the proposition that only such a trusting creditor was entitled to protection against a non-recorded chattel instrument, for only they could be said to have been harmed by the lack of recording, and since the Federal Tax claim was not that of such a trusting creditor — and the Trustee in Bankruptcy was not such a creditor — the Petitioner did not, in any event, bring himself within the purview of protection afforded by the Maryland law.

This point was not passed upon by the State Court, but a determination on that point would likewise render moot the contentions of the Petitioner in this case, since it is conceded also that, notwithstanding any other ruling, unless the Petitioner could bring himself within the protected classes contemplated by the State recording statute, he could not prevail on any ground.

We refer to these matters in order that this Court might have before it the full dimensions of this case, which do not appear from the Petition for the Writ submitted to the Court.

NO GROUNDS EXIST FOR THE GRANTING OF THE WRIT.

ARGUMENT

I.

THE MARYLAND COURT OF APPEALS CORRECTLY DECIDED THE ISSUE PRESENTED IN PETITIONER'S QUESTION NUMBER ONE.

The tax Statute (quoted on Page 11 of App. A by Petitioner) explicitly specifies that it is only after neglect or refusal to pay "after demand" that a tax lien arises, and when it does it applies only to the property and rights to property "belonging to such person". Not only is the mandate of that Section unmistakenly clear, but the factual testimony in the record below demonstrates that those charged by the Internal Revenue Service with tax collection procedures are familiar with such requirements and that a long continued administrative practice has been developed. The tax demand forms prepared by the Government for use in this connection also carefully provides a space for the amount of any interest which may be demanded. All of this is cogently analyzed and verified in the State Court's Opinion on Pages 20 and 21 of Petitioner's Appendix.

Petitioner cites no authority in support of his contention. He suggests that the taxpayer is charged with knowledge that interest runs from the date the tax is due; but this merely serves to concede that there may be a *tax claim*, separate and apart from a *tax lien*, as the Statute

directs the particular procedure by which alone a "tax lien" may arise. Even with regard to the amount of "taxes" (as distinguished from "interest" on such taxes), though the specific amount of such "taxes" be known to the taxpayer, a lien will not arise unless the amount is first demanded and payment thereof neglected or refused. In the absence of a demand, and it is here conceded that there was no demand for interest, a tax lien does not arise.

As a matter of fact, and this too is admitted, when the August 22, 1956 demand for payment of taxes was made in this case, upon which it is now claimed interest would accrue (even though not demanded), all of the taxes so demanded *had already been fully paid and no part of such taxes were then due.* The Tax Collector had acted in error, in making the demand for tax payment, since the very taxes then being demanded to be paid had in fact *already been paid*, and this error, acknowledged to have been made, is the act upon which the Trustee in Bankruptcy relies as the basis for his action in this case. The history and developments attending this matter are outlined in the Opinion of the State Court on Page 20 of the Petitioner's Appendix B. Had the Collector not been misled by his own office, it would appear, since the taxes had already been fully paid, that a demand would not have been made. The original action instituted by the Trustee, it may fairly be said, traces back to this original error of the tax Collector.

Included in the erroneous and mistaken demand, apart from the amount of taxes already fully paid, was a claim for a penalty for alleged late filing (which tardiness was disputed), an item which is of no consequence in this case, by concession of all the parties, since penalties do not become provable claims in bankruptcy (Petitioner's App. B — Page 21).

Question Number One, as submitted by Petitioner, turns upon a finding of fact by the Court; this appears in the Court's Opinion, with a complete analysis of the undisputed facts, at Pages 20 and 21 of Appendix "B", filed with the Petition in this case.

The Appellate Court collected and discussed in its Opinion the important cases (Pages 22 and 23 of Petitioner's App. B) which have considered the necessity for this statutory demand, in order that upon neglect or refusal "to pay the same after demand" a statutory Federal tax lien may be created.

II.

THE DOCTRINE OF "RELATION BACK" (PETITIONER'S QUESTION NUMBER TWO) HAS NO APPLICATION IN THIS CASE.

Evidently, this Question is depended upon by the Petitioner as justifying the issuance of the Writ, for he virtually concedes the correctness of the Lower Court's decision (on his Question Number One) respecting the necessity of a demand antecedent the creation of a tax lien, in the opening words of the second paragraph of Page 7 of his Petition.

The Petitioner then suggests that his "relation back" theory, under certain circumstances, overcomes the lack of prior demand. The plain wording, of course, of Section 6321 of the Internal Revenue Code requires that interest be demanded before "the amount" thereof shall become a lien. In support of this argument the Petitioner cites several cases, but it will be found that they are not pertinent to the Question presented here, nor applicable to the circumstances of this case.

In all of those cases the property sought to be affected was in the possession of the Trustee in Bankruptcy (Fidelity Tube Corporation), or in the possession of the Estate of the deceased taxpayer (U.S. v. Ettelson). In our case, the proofs of claim upon which the Petitioner depends as the basis for invoking his theory of "relation back" were first filed more than sixteen months after the property, sought to be subjected to the alleged lien, had been completely sold to bona fide purchasers, and many months after that sale had been finally ratified by the Court, whose officer sold such property.

The Petitioner, in framing his Question Number Two (Page 2 of his Petition) incorporates as "A." the further theory that the requirement of demand, written into the Tax Statute, may be waived by the taxpayer. No authority is cited to support this particular contention. The instant case, unlike those which are cited by the Petitioner in his discussion of his other theory of "relation back", to which his reference to a waiver by the taxpayer is coupled, did not involve merely the Tax Collector and the taxpayer, but the property rights of third persons, and it is not conceivable that an alleged, though unproven, act of waiver by the taxpayer could disturb or prejudice the property rights of third persons, whether they be bona fide mortgagees, bona fide purchasers or others, or for that matter supply the essential procedural step specified by Congress as a condition to the creation of a statutory tax lien.

The State Court has ruled that the foreclosure sale was validly made and that the sales were properly ratified, and therefore when the first of the alleged tax liens was filed, under prevailing State law, there was no property nor any right to property belonging to the taxpayer (Bankrupt). Neither *Fidelity Tube* nor *Ettelson* is authority for the proposition that a demand, first made at a time when the

taxpayer, under State law, no longer has any property interest, can be used to "relate back" so as to create a lien against an interest which was long before validly and effectively extinguished.

This contention, we submit, disregards the realities. It would permit the Petitioner to create, much later and long after the total disappearance of any property or interest in property in the taxpayer, a fictitious lien so as to seek to subject the chattels in the ownership of bona fide purchasers to a lien which had no existence when they became such purchasers, solely on a theory of "relation back". It is difficult to imagine a more frightening example of disregard of constitutional or orderly process.

The *Fidelity Tube* case (278 F. 2d 776) was marked by a very vigorous dissent by two Judges in that case, who pointed out that the majority decision, even under the circumstances of that case, not only disregarded the statutory prerequisite of a "neglect or refusal to pay", but also did violence to the pattern of priorities set forth in the Bankruptcy Act, and violated the long honored principle that the filing of a Petition in Bankruptcy operates as a cut-off date for the creation or perfection of liens (at Pages 788-91 of 278 F. 2d). The majority in this case, in which the property was still in the possession of the Trustee, relied primarily upon a single decision which had no relationship to Bankruptcy proceedings (Ettelson), while at the same time recognizing that other Federal Courts had reached contrary conclusions, even in Bankruptcy cases. See *In Re Crockett*, D.C. N.D. Cal., 1957, 150 F. Supp. 352, and *In Re Holdsworth*, D.C. N.J., 1953, 113 F. Supp. 878, both cited at 278 F. 2d 776, 780.

In the *Ettelson case*, 159 F. 2d 193 (7th C.A. — 1947), also cited by the Petitioner, the Government's demand definitely embraced, as a part of the combined amount,

the tax deficiency and the interest computed thereon; the supporting assessment list established that interest had been separately assessed (159 F. 2d at 195), and the demand (which, in the Ettelson case, consisted of the filing of the claim in Probate proceedings — while the property was still in the possession of the decedent's estate) referred specifically to the supporting assessment lists, indicating that a demand had been made for interest (159 F. 2d at 196).

The relation back theory of the Petitioner also disregards the statutory requirement that the demand must antedate the refusal to pay, as it disregards also the fact in this case, which is without dispute, that the demand for a "tax" payment here was first made when there were no "taxes" to be paid and consequently none which could be demanded to be paid. It ignores the administrative practice just as it rejects the purpose and format of U.S. Treasury Department Form 17, which is so fully discussed in the Opinion of the Court below (Petitioner's App. B — Page 20).

III.

THE RECORDING OF A FEDERAL TAX LIEN AFTER VALID FORECLOSURE OF THE CHATTELS DESCRIBED IN A PRIOR CHATTEL MORTGAGE DOES NOT SUBJECT SUCH CHATTELS TO THE SUBSEQUENT TAX LIEN, EVEN THOUGH THE CHATTEL MORTGAGE IS NOT FORMALLY RECORDED.

The Petitioner, in urging this Court to consider the issuance of a Writ, on the ground set forth as his third contention, overlooks many salient facts and also ignores the opinion of the State Court in this case.

This Question of the Petitioner suggests that the chattel mortgage must for all time be treated as unrecorded (it was recorded in one jurisdiction, which the Court below ruled was not the proper place for recording), even though

sixteen months or more before the Trustee in Bankruptcy came into being the chattels had been fully taken into possession by the mortgagee and even though they had been completely sold to bona fide purchasers at least sixteen months before the appearance of the Trustee in Bankruptcy.

Eminently noteworthy here must be the fact that this is really a collateral type of appearance, since, notwithstanding his knowledge of this case, the Federal Tax Collector does not advance any of the contentions submitted by the Trustee in Bankruptcy.

We have invited the Court's consideration to the pronouncement of the State Court that such act of possession by the mortgagee might be considered as equivalent to formal recording. Attributing to such possession the equivalence of such recording, and this is a matter for State determination alone, we find that while the tax lien was still unrecorded when the chattels were sold, the mortgage, in compliance with State requirements, had achieved a status equivalent to recording.

The tax lien contemplated by Section 6323 of Internal Revenue Code, is one which, upon filing of the tax lien, may subject "property and rights to property" belonging to the taxpayer. The State Court ruled that the sale at foreclosure, which antedated the filing of any tax lien, finally and effectively established that the taxpayer had no property or interest in property in such chattels. These are matters which are traditionally to be determined by State law. The highest Court of Maryland has ruled that there were no rights in property to which the tax lien could attach when the tax lien was filed, as the Statute required it must be, before it attained the status of a recorded tax lien in respect of purchasers or mortgagees.

The Federal tax lien Statute (Sec. 6321 of Title 26 of the United States Code, Annotated) limits its application, in cases in which a tax lien is actually created, to "property and rights to property, whether real or personal, belonging to such person", but it does not purport to fasten such a lien on property or the proceeds of property in respect of which there is no such property right held by the taxpayer. This Federal tax Statute does not create property rights; such rights are created or recognized only by State law. The State Court in this case ruled that under State law the taxpayer did not have any property or rights in property which could be subjected to a tax lien at the controlling date. See the Court's discussion at that portion of its Opinion appearing on Page 19 of Petitioner's App. B.

The decisions to which the State Court referred in its Opinion (Page 28 of App. B of the Petition herein) dealt, as we do here, with interpretations concerning State recording statutes, the purpose and meaning of which and the effect flowing from a failure to observe which are questions purely of State law — Collier, Vol. 4, Paragraph 70.79, p. 1618.

We do not deal in this case with a situation in which the argument is made that Sections 6321-23 of Internal Revenue Code might *subordinate* a State defined unrecorded mortgage to a valid general Federal tax lien, though subordination, of course, would require subordination only of so much as would be necessary to satisfy the amount of the tax lien (in the instant case, the Petitioner deals with a sum of approximately $13.00 of alleged interest lien, while the mortgage sale proceeds here exceed $148,000.00). Even so, "subordination" (which concerns itself with "priorities" only) would not render such a mortgage "fraudulent as against" or "voidable by" the Federal Government and bring about the situation commented

upon in the Opinion below (Page 18 of App. B.). Particularly, as the State statute does not permit unsecured creditors to challenge even an unrecorded chattel mortgage, would such an anomalous result do violence to the purpose of Maryland's recording statutes. Neither does the State recording statute, as construed by its courts, classify even an unrecorded chattel mortgage as "fraudulent" or "void" or "invalid"; it simply as an unrecorded instrument, must yield its priority to the extent necessary to allow payment of the other lien. See, *Plaza Corporation v. Alban Tractor*, 219 Md. 570 at 588 (cited below in that segment of its Opinion shown at Page 14 of Petitioner's App. B).

Even were this case one which involved a contest between an unrecorded but valid Federal tax lien and an unrecorded, though choate contractual chattel mortgage, we contend the latter would prevail. The Court's ruling in *United States v. R. F. Ball Construction Co.*, 355 U.S. 587, also referred to in the Opinion of the Appellate Court (Petitioner's App. B — Page 27), involved an assignment by a sub-contractor to a surety company, and not a contractual chattel mortgage, for a fixed sum, with full choateness, and was evidently treated by the majority as an inchoate instrument rather than as a contractual chattel mortgage. The dissenting Justices, considering that, despite the form was that of an assignment to a surety, it should be treated as if it were a chattel mortgage, and that as such a chattel mortgage, though unrecorded, it was superior to the Federal tax liens, even though the latter were recorded.

The instrument in this case is a true contractual chattel mortgage — it was fully choate and it has been held to have been a valid chattel mortgage under Maryland state law. (See, Opinion of State Court appearing at Page 23 of

Petitioner's App. B.). Moreover, the State Court, as we have noted, indicated that the mortgagee's possession, prior to the filing of the Federal tax lien, was equivalent to recording, and in that posture the instrument in our case may be regarded as a recorded chattel mortgage.

In *United States v. Ball*, the Tax Collector was directly asserting a lien against property which was then in existence, and which belonged to the taxpayer at the time of the filing of the Federal tax lien. None of these elements are present in this case.

The State Court referred (at that place in its Opinion which appears at Pages 27 and 28 of Petitioner's App. B) to some of the post-*Ball* cases, in which the conclusion was reached that a choate and contractual mortgage, even though unrecorded, prevailed against a Federal tax lien, even though recorded. The expressed purpose of the Federal Tax Statute was to enable the Collector to reach property "belonging" to the taxpayer but only such property. Where the bona fides of, and the existence of, a choate mortgage instrument coincided, the Collector does not prevail over the holder of that prior mortgage. The Alban mortgage was bona fide, was choate and long antedated the tax assessment (passing, for the moment, the clerical error which gave birth to the assessment and to the further fact that the Collector was not a "trusting" creditor). Perhaps, no legal or equitable principle is more honored in our jurisprudence than that which recognizes that "first in time is first in right".

CONCLUSION

The Petitioner, apart from the merits of the controversy, has failed to present any compelling reason why this Court should grant Certiorari in this case. There is no conflict in the Circuit Courts of Appeal. There is no Federal ques-

tion of substance. This case involves determinations of matters of fact peculiar to this case and the case below turned, basically, upon questions exclusively within the province of the State Court to decide. Beyond all this, the decision of the Appellate Court, even should Certiorari be issued, is sustainable on any remand by that Court exclusively upon State grounds. Additionally, there is the pointed indication, that under State law — which is controlling on this proposition — the chattel mortgage is to be treated as though it had been recorded, since possession of the chattels was taken prior to the filing of a Federal tax lien and that such possession is the equivalent, in Maryland, of recording.

For the reasons stated, it is respectfully submitted that no useful purpose can be served by granting the Writ of Certiorari in this case.

Status of Plaza Corporation

We do not know at this time whether the third Respondent, Plaza Corporation, will submit a Brief in this case, but it should perhaps be drawn to the attention of this Court, as a factor which was noted by the State Court (and by the Trial Court) that Plaza's interests in this case, though it is designated herein as a Respondent, would prompt it to support the contentions of the Petitioner for the Writ in this case (App. B., page 18, footnote).

Respectfully submitted,

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named Respondents.

APPENDIX

Annotated Code of Maryland (1957 Edition):

Article 21, Section 41 (as amended in 1949):

"No personal property, of any description whatever, whereof the vendor, mortgagor, or donor shall remain in possession, shall pass, alter or change, or any property therein be transferred to any purchaser, mortgagee or donee, *as against subsequent* (1) *purchasers*, (2) *mortgagees*, (3) *incumbrancers*, (4) *landlords with liens*, (5) *pledgees*, (6) *receivers*, *and* (7) *creditors who acquired a lien by judicial proceedings on such personal property*, unless by bill of sale or mortgage acknowledged and recorded as herein provided; but nothing herein shall be construed to extend to and sale or gift, where the same is accompanied by delivery, nor gift, where the same is accompanied by delivery, nor to invalidate such transfer as between the parties thereto." (Italicized portion added by 1949 amendment, numbers inserted for convenience).